Agricultural Outlook Forum 2000

Speech Booklet 3

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10:30 PANEL ON THE FUTURE OF BIO-ENGINEERED FARM PRODUCTS
Biotechnology, A Farmer's Perspective
Douglas D. Boisen, President, Boisen Farms, Inc., Minden, Nebraska

2:15 THE PROS AND CONS OF PRODUCTION AND MARKETING CONTRACTS
Lessons from the Hog Industry's Experience with Contracting
Jon Caspers, Member, National Pork Producers Council Board of Directors, Swalesdale, Iowa

4:00 CONCENTRATION AND STRUCTURAL CHANGE IN AGRICULTURE
Antitrust Enforcement and Agriculture
Douglas Ross, Special Counsel for Agriculture, Antitrust Division, U.S. Department of Justice
The Case Against an "Agrarian Antitrust Policy"
F. R. Warren-Boulton, Principal, MiCRA: Microeconomic Consulting and Research Associates, Washington, D.C.

BIOTECHNOLOGY, A FARMER'S PERSPECTIVE

Douglas D. Boisen
President, Boisen Farms, Inc.
Minden, Nebraska

I want to start by asking a question: Can anyone tell me who this quote is attributed to--"This corn is going to kill agriculture." If you said a French farmer talking about hybrid corn introduction in France in 1950, you are right. So, the fear of new technology is nothing new.

Currently, bio-tech seeds that are available today appear to have more producer benefits, but I believe the next round of bio-tech introductions will offer the starving and malnourished of the world new hope and salvation. As an example of this, a new bio-tech rice has been developed that is higher in Vitamin A and iron. This year alone 1/2 million children will go blind from lack of vitamin A, and iron deficiencies are responsible for anemia in millions of women and children. I feel that it is our moral responsibilitiy to do everything we can to insure that more of these products become available to every farmer in the world.

The whole story of bio-technology is not being told, it is not just a crop issue. Bio-tech enzymes have been used in detergents and cheese-making for more than a decade. Bio-tech yeast is used in making bread, beer and wine. Bio-tech medicines save lives everyday. But, I'm here to talk about one farmer's perspective on bio-tech crops.

I have received many messages from Agriculture in the last 30 years. The one message that has remained constant for all that time is: "You have to become more efficient in order to stay in business." This is a message that producers take very seriously and work very hard to achieve.

I believe our desire to become more efficient is the reason we not only accept but embrace new technology. Every farmer has to evaluate any new technology to determine whether it will do one of two things for his or her operation: (l) lower production costs while maintaining yield or (2) increase yield while maintaining production costs.

Bio-technology is no different than any new technology that farmers employ, but evaluating bio-tech is a lot more demanding. There are many factors that have to be considered and the uncertainty of where this technology is going is always a constant worry. Take for example BT corn on my irrigated farm in Nebraska. I have a lot more to evaluate than the technology fee for BT vs costs of chemical treatment for corn borer control on conventional corn. If I choose to plant BT corn, I have made a decision to treat for corn borer that may or may not occur at an economic treatment level 6 to 10 months in the future. Currently, this tech fee runs about $10 per acre.

I have to be sure that any variety I plant is approved for export, or will be used domestically. In Nebraska, we produced a little over 1.2 billion bushels of corn in the 98/99 marketing year. Of that we used 577 million bushels in-state and exported 575 million bushels. Of that 575 million bushels, only 230 million bushels left the United States. So, you can see that foreign exports are a small but very important part of our business. I am constantly aware of the fact that the rules for sale of my corn that are in place

during the spring when I'm planting may be changed completely by the fall when I'm harvesting. Sometimes I feel my odds would be better in Las Vegas.

As a producer, I get very frustrated with what appears to be public concern over bio-technology. I blame the radical environmental groups for the misinformation that is offered and the media for playing it up so it sells better. The questionable report on the Monach Butterfly got a lot of media attention, but when was the last time you read an article about the environmental benefits? BT corn contains a protein from a soil organism which is very effective against European Corn Borer but is harmless to other living things--birds, fish, mammals and most beneficial insects. Another big benefit to me is farm safety. I don't have to handle and be exposed to commercial insecticide to control corn borer. Another benefit for all of us is the use of less chemicals. Water quality will also improve. This story is not being told.

The American farmer is very proud of the fact that he not only feeds himself but also 135 other people. With world population at 6 billion plus, and with the expected growth in the next 20 years, the most conservative figure I've seen is 8 to 9 billion...we have a problem! We need to produce for a lot more than 135 people and bio-technology can help us meet these challenges of tomorrow. In an article in the Washington Times dated November 15, 1999, Secretary of Agriculture Dan Glickman, was quoted as saying, "Today, in a world of growing population and shrinking farmland and forests, biotechnology becomes that much more important. We have more and more people to feed, more and more fiber to produce, and a limited amount of arable land to put into production."

In closing, I can tell you that I believe in and trust biotechnology; and yes, I do plant bio-tech seeds on my farm, when and where I feel it will be profitable!

LESSONS FROM THE HOG INDUSTRY'S EXPERIENCE WITH CONTRACTING

Jon Caspers, Member
NPPC Board of Directors
Swaledale, Iowa

The pork industry now has ample experience with both production and marketing contracts. We have seen both good and bad sides of these arrangements and, regardless of what any individual thinks of them, are convinced that they are part of the permanent landscape of animal agriculture. We firmly believe that correctly structured, negotiated contracts can serve all parties well in developing a closely coordinated pork industry that is competitive with any meat protein industry in the world. The point of debate at this point is whether these contracts have been structured to create win-win situations for contractors, growers and packers. The results to date are decidedly mixed.

The first and foremost idea that I want to get across today is this: Pigs are not chickens are not vegetables. Every product, even those which are close competitors such as pork and broilers, is unique and must be treated uniquely. Analysis or policies appropriate for one may be entirely inappropriate for another. It is paramount that we all keep this in mind. We in the pork industry are especially sensitive on this point since it seems that activist groups are incessant in their attempts to foist the problems of the broiler contracting system on the pork industry. The animals are different. The systems are different. The markets are different. The people are different. Treat us differently because we have fewer and different problems.

The second idea that I want to convey today is that while poultry production contracts embody marketing contracts, these two are still almost completely distinct in the pork industry. Yes, one can turn into the other when you think about a marketing contract really being another way to get someone to raise pigs for a processor. But pork production contracts have historically been initiated by a producer (sometimes a very large one, but a producer nonetheless) with sows who wants to grow pigs to market weight or grow more pigs. Conversely, marketing contracts have been initiated by either a producer or a packer with the explicit purpose to transfer pigs in a manner that guarantees shackle space and hog supply, respectively.

With this distinction in mind, I will address what I believe the pork industry has learned about production and marketing contracts separately.

Production Contracts

The number of hogs farrowed and finished under contracts has grown steadily over the past 20 years. There are good reasons for this growth. Production contracts:

- Are hardly ever lowest-cost production options. The major reason is simple: Contractors have to pay for the buildings again and again even after they are depreciated out. In addition, the geographic separation of contract sites and the need for supervision add administrative and logistical costs. Some of these are no doubt offset by economies of scale in genetics procurement, feed manufacturing and marketing but all of the data to date suggest that production can be done for

less cost in owned buildings than in contracted ones. Contract production is cost competitive but not lowest cost.

- Are used effectively as a rapid expansion strategy -- This is a way to grow a business by accessing someone else's equity and credit line. It allows contractors to invest their money in the most productive asset, pigs, and entice someone else to invest in a less productive but less risky asset, buildings.
- Are an effective way to secure labor that has a stake in the performance of the operation. And this factor may get more important as labor supplies tighten, especially in the Midwest.
- Allow contractors to achieve the geographic dispersion needed to provide bio-security and spread environmental risk. In addition, contract facilities can place waste nutrients nearer to target cropland without requiring the contractor to buy large tracts of land. This adds value to the waste nutrients, frequently enough to generate positive contribution margin from these waste nutrients.
- Provide a diversification and entry opportunity for many rural families and do so while giving them much needed management support, access to modern genetics and market access.

I would classify the pork industry's experience with production contracts as widely successful. We have seen few of the problems that have been so widely publicized in the broiler industry, mainly because of the ease with which weaned pigs, feeder pigs and market hogs can be transported. Because of this ease, no contract grower is captive to a single contractor. This gives growers options to negotiate better contracts and keeps contractors honest and aggressive in their dealings with growers.

Pork contractors (especially the large ones) have invested much effort in building up reputational capital in areas where contract production is widespread. Virtually all of them count reputation as an asset that cannot be put at peril. There have been cases of default on production contracts but, to our knowledge, few of them have involved the large contractors whose every move is watched closely and publicized widely.

Finally, pork contractors, unlike broiler contractors, cannot afford to lose growers and their buildings because production decisions are made months in advance. The flow of pigs cannot be turned off in three weeks as can the flow of broiler chicks simply by deciding not to put eggs in an incubator. This longer planning horizon is also the reason for pork production contracts being much longer term agreements than what I consider the ridiculously risky flock-to-flock system prevalent in the broiler industry.

The lack of geographic monopolies on the part of contractors may not always be the case, especially if the mergers of 1999 continue. But the characteristics of the pork production system and the continuing need for high quality farrowing and finishing facilities suggest that contract growers of hogs are not as likely to become as captive to or as disposable by contractors as are their counterparts in the broiler industry. And, as of today, it doesn't appear that the one "surplus" facility that in essence floods the market has yet been built so the market for contract growers and barns remains generally tilted to the sellers' side.

Marketing Contracts

The real contribution of the pork industry to a "What have we learned" discussion is, no doubt, in the area of marketing contracts. NPPC is supportive of producers' rights to decide whether they need a contract to guarantee market access and manage price

risk. We see contracts as a viable alternative for coordinating systems which neither the producer nor the packer want to vertically integrate and to make these systems competitive. We are also convinced that the first generation of marketing contracts, many of which are about to expire, are not fair enough to both sides to accomplish these goals.

First, a bit of history. Marketing contracts were developed by packers in response to producer requests. It was producers, not packers, who first proposed marketing contracts in an effort to guarantee access to slaughter capacity and, in many instances, to reduce price or cash flow risk. As a few packers responded, others quickly developed their own programs in order to prevent their competitors from tying up the supply of good, lean hogs. In the early days of market contracts quality was a key driver -- packers wanted to secure the best hogs.

In the rush, many mismatches between producer goals and contract features were created. Many producers who, after the slaughter capacity problems of the fall of 1994, were concerned about having a place to sell pigs signed contracts that included price risk management when they neither wanted nor needed that feature. Others signed formula contracts that they erroneously believed would affect the average price received enough to offset the risk posed by price variation. Still others signed contracts, which put floors under prices and included a "ledger" feature that they believed would never get too large and would self-liquidate over time. So they believed!

All of these contracts were written buy the packers. Some had terms that were somewhat negotiable. Others were strictly contracts of adhesion or "take it or leave it" deals. As with any contract, the party that wrote these (i.e. the packers) made sure that their interests were taken care of. Many terms gave them unilateral power to change everything from quality standards to delivery to the pricing matrix itself. All were predicated on "historic" hog cycles and price levels and this doomed them to problems in a market like that of late 1994 through 1999.

So what have we learned. Quite a bit and most of it has not been pleasant. Here are the highlights:

- History doesn't always hold OR make sure you look at ALL of history. Did anything really suggest $10 hogs in the fall of 1998? No. But nothing really suggested that hog prices would stay in the $35 to $60 range of the '80s and early '90s either. If all of history is considered, the possibility of lower priced hogs was clear. Was it "probable" in today's world? Again, no. But probability distributions theoretically contain every possible outcome, including positive and negative INFINITY. Never think it will never happen. The result of this narrow view of history is huge ledger balances that may never be repaid. The lesson is for producers and packers to consider the full range of possible outcomes and develop adequate contingency plans. These are, at least in theory, long-term and supposedly win-win relationships.
- Producers should match contract provisions to their critical needs. If market access is the key issue, then agree to supply hogs to packer A in turn for packer A agreeing to take your hogs on a timely basis and leave price risk management up to the separate parties. The lesson is for producers to carefully analyze what is actually needed and negotiate for only those features. The arrangements must be win-win or no deal.

- Be wary of any contract clause that gives one party (usually the contract writer) the unilateral power to change a contract provision. The ability to change business relationships is needed but the changes should be the result of negotiation, mediation or, as a last resort, arbitration. Our experience with packers changing weight discount ranges, leanness premiums and a host of other items at their own whim has been entirely negative and will probably be played out in more than a few courtrooms over the next few years. The lesson here is to carefully review contracts and develop alternative to the unilateral change provisions. Change is often a necessity, but leaving the decision in one parties hands is a recipe for disaster. The need for change should be a signal for renewed negotiation and, if a mutually acceptable decision cannot be reached, possible mediation or arbitration.
- Provide for changes in government services and information. A main source of unhappiness with contract performance has been packers' decisions regarding base prices after the USDA-AMS changed their price reporting system in 1999. And at least one packer chose to use a reported price that was clearly in the packer's favor in spite of ample data demonstrating a method of mimicking the discontinued "Iowa-Southern Minnesota Practical Top" price report. The only recourse to producers to react to what they consider was a breach of contract was to breach the contract them selves and sell hogs on a $20 cash market. Some recourse! The lesson here is to include the possibility of information changes in the contract and spell out how such changes will be handled. Again, negotiation, mediation and/or arbitration are all possible courses of action.
- Be very careful about narrowing the market that serves as the base for a large percentage of the contracts in force. Many of today's contracts use the Iowa-Southern Minnesota 10:30 a.m. report to price a given day's purchases or deliveries. So, the price of all of these contracted hogs is determined by purchases occurring before 10:00 a.m. on a given day. In addition, a good portion of the contracts is priced at the midpoint of the range of prices reported at 10:30 a.m. These contracts are priced on an even narrower set of hogs -- the highest and lowest priced lots sold before 10:00 a.m. on a given day. As the base market is narrowed more and more, the more open to manipulation it becomes. And when producers have tried to take an active role and report the prices they receive to AMS, many have found it impossible to get a bid on their hogs before 10:00 a.m. but easy to get bids at higher prices after the 10:30 a.m. report. We believe it is blatant manipulation but we also admit it was our own "collective" doing that made it possible. The lesson here is to be careful about the scope of the price determining market. One of the best features of the impending Mandatory Price Reporting system is its inclusion of a prior day report that will include ALL of the hogs purchased by plants which slaughter over 100,000 head per year. These data, since they are on such a broad set of hogs, will be practically impossible to manipulate. Furthermore, the records and enforcement provisions of the Mandatory Price Reporting Act promise to make the data accurate and hold packers accountable for such accuracy.

So what should the response be? Regulation is a possibility but not one that we are extremely fond of. Standardized disclosure requirements would reduce confusion and facilitate comparisons and competition. The catalog of contracts required by the Livestock Mandatory Price Reporting Act of 1999 will help producers be aware of what is available to them.

But the most important action to be taken is for producers to learn more and be more vigilant about their business dealings. It is unbelievable the number of producers who

admit that they never had their attorney review the marketing contract that they signed. It is shocking how many producers never read the contract themselves. This is just lousy business practice that must end in today's more sophisticated world. The courts will not likely remain sympathetic forever to producers who do not follow sound business practices.

We at NPPC have recently assembled a committee of experts to review marketing contracts and write what we believe to be a much-needed and valuable addition to the pork producers' decision-making arsenal. NPPC's Guide to Marketing Contracts will be publicly available for the first time in two weeks at the National Pork Industry Forum in Kansas City. It covers many of the issues I have discussed today and demonstrates the performance of the various marketing contracts over recent years. It is not meant to be legal advice but is meant to stimulate what we believe to be the correct and necessary questions that producers should ask themselves and any packer who offers a contract.

I appreciate the opportunity to discuss these issues with you today and hope that you better understand the pork industry's experience and education regarding contracts. I look forward to responding to any questions.

DEPARTMENT OF JUSTICE

Antitrust Enforcement and Agriculture

Address by

DOUGLAS ROSS
Special Counsel for Agriculture
Antitrust Division
U.S. Department of Justice

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I am pleased to have the opportunity to discuss the role that the antitrust laws play in the agricultural marketplace. In the last few years, agricultural producers and others have expressed concern about competitive conditions in the agricultural marketplace, about the impact on farmers of particular mergers and acquisitions, and about levels of concentration in agriculture generally. We know that the agricultural marketplace is undergoing significant changes, including major advances in technology and productivity, changes in business relationships between producers and packers/processors and, in certain sectors, increasing concentration.

As recent actions by the Antitrust Division demonstrate, we hear the concerns being expressed and take them very seriously. By any measure, the Division has been spending a significant amount of time, energy, and resources on agricultural issues recently. Sometimes our work results in enforcement actions, a few of which I will describe shortly.

Perhaps the most recent Division actions – apart from case filings – reflecting both that it hears these concerns and that it takes them seriously are Assistant Attorney General Joel Klein's announcement last year that he would create within the Division a new position of Special Counsel for Agriculture and his fulfillment of that promise with my appointment. Assistant Attorney General Klein has asked me to draw upon my quarter-century experience in antitrust and litigation at the state and federal levels to focus full-time on the agricultural marketplace and to provide him assistance and advice to supplement the Division's ongoing antitrust enforcement efforts. Mr. Klein has also personally traveled to the Midwest twice in the last year to visit with large groups of farmers, to hear their concerns directly and to improve everyone's understanding of how the antitrust laws operate and how the Division works to protect competition under them. Over the last several years, other Division officials have met with individual farmers and agricultural organizations and testified at hearings here in Washington and in the field as well to hear these concerns and to explain how the Division's mission to enforce the antitrust laws applies in the agricultural sector. Let me now turn to those topics to give you a better understanding of the work of the Antitrust Division.

The role of the Antitrust Division in the midst of the changes faced by the agricultural marketplace is narrow but important: we enforce the antitrust laws. We are not regulators. We do not have the power to restructure any industry, any market, or any company, or stop any practice, except to prevent or cure specific violations of the antitrust laws that we can prove in court. When we bring an action, the court decides whether the antitrust laws are being violated in the particular instance, and whether the remedy we are seeking fits the violation. The court's decision depends on the particular facts in evidence. Therefore, we bring an enforcement action in court only when we are in possession of factual evidence that gives us good reason to believe that the antitrust laws have been violated.

There are three basic kinds of violations of the antitrust laws. First, the antitrust laws prohibit conspiracies to deny market access or otherwise suppress competition. Second, they prohibit the use of predatory and/or exclusionary conduct to acquire or hold on to a monopoly in a market. Third, they prohibit mergers and acquisitions (referred to collectively hereafter as "mergers") that are likely to substantially lessen competition in a market. On a day-to-day basis, the most frequent context in which we consider concentration levels, about which agricultural producers and others express concerns, involves our analysis of mergers. The antitrust laws do not prohibit all increases in concentration. Increases in concentration may occur through internal growth or through mergers. Internal growth, in particular, is generally thought to be economically beneficial, as it most often reflects the success of producers in the marketplace in attracting and satisfying customers. So, too, mergers can be economically beneficial, allowing the resulting entities to operate more efficiently, reduce costs, and better meet the demands of the marketplace.

The antitrust laws are based on the notion that competitive market forces should play the primary role in determining the structure of our economy. The consumer is the primary beneficiary of antitrust enforcement and effective competition among producers of goods and services at all levels in the production process, because that competition leads to better quality, more innovation, and lower prices. This is why it is often said that the antitrust laws protect competition, not competitors. But producers who seek to supply products and services also benefit, because antitrust enforcement and effective competition enable them to do so free from anticompetitive interference. Our job is to stop the specific kinds of private-sector conduct I just mentioned from interfering with competitive market forces.

The antitrust laws protect competition in the agricultural sector of our economy just as they do in other parts of the economy. A number of industries are also regulated by government agencies under statutes that go beyond the antitrust laws to establish additional, industry-specific regulatory requirements and standards. For example, the meat-packing industry is regulated by USDA's Grains Inspection, Packers and Stockyards Administration. While the antitrust laws play an important role in helping keep markets competitive, they will never address all of the complex issues facing American agriculture in this time of change. That is why the government continues to focus on a broad range of agriculture policy issues.

What the Antitrust Laws Prohibit

A minute ago, I referred to three different types of antitrust violations. Let me state them more specifically. First, it is a violation of section 1 of the Sherman Act for separate firms to agree among themselves not to compete with each other, but instead to join forces against their

consumers or their suppliers. Second, it is a violation of section 2 of the Sherman Act for a firm to monopolize or attempt to monopolize a market. Third, it is a violation of section 7 of the Clayton Act for a firm to merge with another firm or acquire its assets if to do so would be likely to substantially lessen competition in any market. I'd like now to describe each of these types of violations in a little more detail, and give you an idea of how we approach each of them.

1. ***Collusion***

The first type of antitrust violation, when firms that are holding themselves out to the public as competing against each other instead agree with each other to unreasonably restrain competition among themselves, is often referred to as collusion. Collusion is a willful subversion of the normal operation of free markets, and can result in serious harm to consumers, suppliers, and the economy. It virtually always results directly in inflated prices to consumers, or depressed prices to suppliers, and in denial of choices in the marketplace; indeed, that is its purpose. The most common types of collusion are agreements to fix prices, agreements to allocate markets, and agreements to boycott particular customers, suppliers, or competitors.

Price fixing can include agreeing on the specific price, or rigging a specific bid, but it can also include agreeing to increase or depress price levels, or agreeing to follow a formula that has the intended effect of raising or depressing prices or price levels. Allocation of markets can include agreeing to divide up geographic areas to avoid competition, or agreeing to divide up customers or suppliers within an area, or agreeing to divide up a sequence of bids. Group boycotts can include any agreement among competitors that they will deal with their customers or their suppliers only on particular terms, in order to suppress competition.

This summary oversimplifies the full range of Section 1 violations. There are other kinds of such violations where the anticompetitive intent and effect may be less clear-cut. But all section 1 violations share the same basic characteristic, that firms who are supposed to be independent actors in the marketplace are instead agreeing to join forces to restrain competition.

It is important to remember that with any of these forms of collusion, proving a case requires evidence of an agreement between the firms in question. Absent direct or circumstantial evidence that the firms are not making their decisions independently, it is not enough to show merely that two agribusiness firms, for example, bid the same price for a commodity, or that one tends to buy in one area and another tends to buy in another area. What would concern us is if there were additional facts showing collusion directly or circumstantially, such as patterns of bids over time, or patterns of attendance at various sales or auctions, that didn't make competitive sense – that couldn't be explained as part of normal competitive behavior. Needless to say, if we obtained reliable evidence suggesting agreement, such as two firms discussing with each other what price they intend to bid or accept, or where they plan to focus their buying or selling, we would definitely be concerned and look into it.

Let me mention three collusion cases we have brought recently. The first one I'll mention is our criminal prosecution against Archer Daniels Midland and others, beginning in 1996, for participating in an international cartel organized to suppress competition for lysine, an important livestock and poultry feed additive. The cartel had inflated the price of this important agricultural input by tens of millions of dollars during the course of the conspiracy. ADM pled guilty, and was fined $100 million – at the time the largest criminal antitrust fine in history, now the third largest. Other participating corporations have also been prosecuted and assessed multi-million-dollar fines. In addition, three ADM executives were convicted for their personal roles in the cartel; last summer, two of them were sentenced to serve two years in prison and fined $350,000 apiece for their

involvement, and the other executive had 20 months added to a prison sentence he was already serving for another offense.

The second collusion case I'll mention is our prosecution of the Swiss pharmaceutical giant, F. Hoffmann-La Roche Ltd., and a German firm, BASF Aktiengesellschaft, for their roles in a worldwide conspiracy, over the course of nine years, to raise and fix prices and allocate market shares for certain vitamins sold in the United States and elsewhere. The conspiracy affected $5 billion in U.S. commerce, involving vitamins used not only as nutritional supplements and food additives, but also as additives in animal feed. In May 1999, the two firms agreed to plead guilty, with Hoffman-La Roche to pay a fine of $500 million and BASF to pay a fine of $225 million. These are the two largest antitrust fines in history – in fact, the $500 million fine is the largest criminal fine of any kind in history. A former Hoffmann-La Roche executive also agreed to submit to U.S. jurisdiction, to plead guilty to participating in the conspiracy and lying to Justice Department investigators about it, and to serve a four-month prison term and pay a $100,000 fine. These prosecutions are part of an ongoing investigation of the worldwide vitamin industry in which there were more than a dozen prosecutions and over $875 million in fines as of the end of 1999.

The third collusion case I'll mention is a much smaller case in monetary terms than the first two; but it is an important one for agricultural producers nonetheless. In December 1997, as the result of an investigation conducted with valuable assistance from USDA, who was also conducting its own investigation under the Packers and Stockyards Act into some of the same conduct, the Department criminally prosecuted two cattle buyers in Nebraska for bid-rigging in connection with the procurement of cattle for a meat packer. Both individuals pled guilty and were fined and ordered to make restitution to the victims.

Before I leave collusion, I should mention an important exception to the prohibition against agreements to restrain competition, found in the Capper-Volstead Act. This law allows producers of agricultural commodities to form processing and marketing cooperatives – in effect to engage in joint selling at a price agreed to by the producer members of the co-op – subject to certain limitations enforced in the first instance by USDA.

2. __Monopolization or Attempt to Monopolize__

Let me now turn to the second type of antitrust violation, monopolization or attempt to monopolize, which is a violation of section 2 of the Sherman Act. For various reasons, this type of antitrust violation occurs less commonly than collusion, but it is also a serious willful subversion of the free marketplace. An example of monopolization or attempt to monopolize would be a dominant company in the market attempting to drive its competitors out of business by interfering with their ability to engage in the business. This might be attempted by the clearly dominant firm refusing to buy from producers who sell to any of its competitors, or refusing to ship with transportation companies who ship for any of its competitors, or refusing to sell to distributors or retailers who handle the products of any of its competitors – if the dominant company in question had enough market power that these refusals would have anticompetitive effects. Monopolization does not require proof of an agreement among two or more firms; one firm can illegally monopolize by itself.

But it is important to understand that monopolization cannot be proved just by showing that a firm has engaged in restrictive conduct. The law also requires proof that the firm has a monopoly – and that requires an extremely high market share all to itself – and that it engaged in the restrictive conduct in order to acquire or maintain the monopoly. Or, in the case of attempted monopolization, it must be proved that the firm has a "dangerous probability" of acquiring a monopoly as a result of the restrictive conduct. And to prove "dangerous probability," the courts generally require, for

starters, that the firm involved in the restrictive conduct already have a quite large market share – a 50-percent share for a single firm might not be enough. And even a 60-to-70 percent market share might not be enough, if other facts indicate that the restrictive conduct involved is unlikely to succeed in creating a monopoly.

Just as important, section 2 monopolization cannot be proved just by showing that the market is highly concentrated. Under our antitrust laws, a firm may lawfully have a monopoly – even 100 percent of the market – as long as the firm has not acquired or maintained that monopoly through the kind of restrictive conduct I described a minute ago, but rather, in the words of Judge Learned Hand, "by virtue of superior skill, foresight and industry."

So both elements – very high single-firm market share, plus conduct to exclude competition – must be proved. One or the other by itself is not enough.

3. __Mergers__

The third type of antitrust violation, a merger that is likely to substantially lessen competition in a particular product market and geographic market, has a different kind of legal standard from the other two, in that it does not require proof that anticompetitive conduct has already occurred. Here, the principal focus is not on the conduct of the merging parties, but on whether the merger would change the market structure to such a degree that competition would likely be substantially lessened. The remedy we seek for a merger that violates the Clayton Act is to sue to stop the merger, or to insist that it be modified to remove the cause for antitrust concern.

Merger reviews require a careful analysis of the markets involved. The Antitrust Division analyzes mergers pursuant to Horizontal Merger Guidelines developed jointly by the Department of Justice and the Federal Trade Commission. The analysis is aimed at determining whether the merger is likely to create or increase market power, or to facilitate the exercise of market power, in any market. Market power is the ability of a firm to raise the price charged to customers – or to lower the price paid to suppliers – a small but significant amount without that move being defeated by counteractive competitive responses by other competing firms moving in to take away those customers or suppliers.

Before we get to that analytical step, however, we must first go through the exercise of determining the scope of the product markets and geographic markets that would be affected by the merger. This is an essential first step in our analysis – until we know the size and shape of the market, we cannot know how big any firm's market share is, for example. The scope of a market is generally defined by the smallest geographic area in which a hypothetical firm, assuming it faced no competition for its product in that area, could make a small but significant change in price stick. Usually, we are looking at that firm as a seller, and determining the smallest area within which the firm's customers would be unable to thwart the firm's inflated pricing by going outside that area for their buying needs. But, as our Merger Guidelines expressly note, we also look at the firm as a buyer, and determine the

smallest area in which sellers to the firm would be unable to thwart the firm's depressed prices by selling to others outside that area – that is, because it would be economically impractical to travel or ship outside that area.[1]

A decision as to the dimensions of this area can sometimes be reached by examining recent buying and selling patterns in the marketplace. But the decision can also depend on a variety of other, more subtle factors, because the ultimate question is not how far the buyers and sellers have traveled or shipped in the past, but how far they could or would travel or ship in response to anticompetitive price changes.

Once we have defined the market, we turn to the question of market concentration and how it would be affected by the merger. There is no automatic threshold of market concentration that will always result in a determination that a merger would violate section 7 of the Clayton Act. Other factors also play an important role in analyzing the impact of the merger – such as other structural features of the market that make anticompetitive effects more likely or less likely; and the ease or difficulty of entry into the marketplace by new competitors who could neutralize any anticompetitive potential. We would also consider the impact of any demonstrable efficiency gains from the merger that would demonstrably result in competitive benefits.

In the recent past, we have reviewed a number of proposed mergers in the agricultural marketplace. The following examples show efforts to protect the interests of farmers as purchasers of corn seed, cottonseed, and farm equipment, and as sellers of grain and soybeans.

In the first seed example I'll mention, in the biogenetics area, in 1998 we investigated Monsanto's acquisition of DeKalb Genetics Corporation. Both companies were leaders in corn seed biotechnology and owned patents that gave them control over important technology. We expressed strong concerns about how the merger would affect competition for seed and, to satisfy our concerns, Monsanto spun off its claims to agrobacterium-mediated transformation technology, a recently developed technology used to introduce new traits into corn seed, such as insect resistance, to the University of California at Berkeley. Monsanto also entered into binding commitments to license its Holden's corn germplasm to over 150 seed companies that currently buy it from Monsanto, so that they can use it to create their own corn hybrids.

In another seed matter, last year Monsanto abandoned its proposed acquisition of Delta & Pine Land Co., which would have combined the nation's two largest cottonseed companies, after

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[1] Market power by a buyer is addressed by the Merger Guidelines under the same analytical framework as a seller's market power that may result from a merger:

> Market power also encompasses the ability of a single buyer (a "monopsonist"), a coordinating group of buyers, or a single buyer, not a monopsonist, to depress the price paid for a product to a level that is below the competitive price and thereby depress output. The exercise of market power by buyers ("monopsony power") has adverse effects comparable to those associated with the exercise of market power by sellers. In order to assess potential monopsony concerns, the Agency will apply an analytical framework analogous to the framework of these Guidelines.

Merger Guidelines § 0.1.

learning of our intention to sue to resolve concerns about the anticompetitive effects of the proposal.

In another agriculture merger case seeking to protect farmers as buyers of farm machinery, last November we filed a complaint challenging the Case/New Holland acquisition as originally announced. To resolve the Division's competitive concerns that the proposed acquisition would likely result in higher farm machinery prices, New Holland Co. has agreed to sell its four-wheel-drive and large two-wheel-drive tractor businesses (part of the nation's $1.5 billion market for agricultural tractors), and Case Corp. has agreed to spin off its hay tool business (the U.S. market for hay tools is about $250 million). Our proposed consent decree is pending in court under a Tunney Act proceeding in which the court makes the final determination that the decree is in the public interest.

In a case where the concerns of farmers as sellers of grain and soybeans were involved, in July 1999, we challenged the Cargill/Continental Grain merger as originally proposed. We were concerned that the proposed transaction would have depressed prices received by farmers for grains and soybeans in certain regions of the country. To resolve our competitive concerns, Cargill and Continental agreed to divest a number of grain facilities throughout the Midwest and in the West, as well as in the Texas Gulf. Our proposed consent decree is still pending before the court. Earlier this month, the Department filed its responses to public comments. Let me give you a sense of the thoroughness with which the Division investigated all the potentially affected markets and sought relief in those markets in which we concluded that the transaction was competitively problematic.

Cargill and Continental operate nationwide distribution networks that annually move millions of tons of grain and soybeans to customers throughout the U.S. and around the world. We looked at all the markets that would be affected by the merger, and concluded that in a number of them, competition would be adversely affected if the assets of the two firms were merged. In this case our concerns included the so-called "monopsony" issue, regarding competition among the two firms as buyers of grain and soybeans from farmers and other suppliers. The lessening of competition resulting from the merger would have resulted in farmers, as sellers, being anticompetitively forced to accept less money for their major crops than before the merger.

Thus here, among the required divestitures, we insisted on divestitures in three different markets where both Cargill and Continental currently operate competing port elevators, to preserve the competition that currently exists for purchasing the grains and soybeans of affected producers: (1) Seattle, where the elevators now compete to purchase corn and soybeans from farmers in portions of Minnesota, North Dakota, and South Dakota; (2) Stockton, California, where the elevators now compete to purchase wheat and corn from farmers in central California; and (3) Beaumont, Texas, where the elevators now compete to purchase soybeans and wheat from farmers in east Texas and western Louisiana.[2] We also required divestitures of river elevators on the Mississippi River in East Dubuque, Illinois, and Caruthersville, Missouri, and along the Illinois River between Morris and Chicago, where the merger would have otherwise harmed competition for the purchase of grain and soybeans from farmers in those areas.

Because we were concerned that the merger would have anticompetitively concentrated ownership of delivery points that have been authorized by the Chicago Board of Trade (CBOT) for

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[2] In addition to benefitting farmers and other suppliers in the above-mentioned states – who can be said to be captive to the elevators involved – the required divestitures may also benefit farmers and other suppliers in Illinois, Iowa, Nebraska, Missouri, Kansas, Oklahoma, Colorado, and New Mexico, who, while not necessarily captive to the elevators involved, nevertheless rely on them as competitive alternatives.

settlement of corn and soybean futures contracts, we required the Illinois River divestitures, and an additional divestiture of a port elevator in Chicago. The futures markets delivery points would otherwise have been under the control of Cargill and one other firm, which would have increased the risk that prices for CBOT corn and soybean futures contracts could be manipulated.

Moreover, we required divestiture of a rail terminal in Troy, Ohio, and we are prohibiting Cargill from acquiring the rail terminal facility in Salina, Kansas, that had formerly been operated by Continental, and from acquiring the river elevator in Birds Point, Missouri, in which Continental until recently had held a minority interest, in order to protect competition for the purchase of grain and soybeans in those areas.[3]

I should note that we received valuable assistance in our review of the Cargill/Continental merger from the U.S. Department of Agriculture, as well as the Commodity Futures Trading Commission, and several state Attorneys General.

Coordination with USDA

The Antitrust Division maintains close contact with the USDA's Grain, Inspection, Packers and Stockyards Administration (GIPSA). GIPSA does not have authority to enforce the Sherman and Clayton Acts, although it does have authority to consider competition concerns as part of its authority under the Packers and Stockyards Act; that authority, by the way, extends beyond conduct that violates the antitrust laws. And if GIPSA uncovers conduct that it believes may violate the antitrust laws, it has authority to refer the matter to us for investigation and enforcement. We and GIPSA share information with each other on a regular basis. For example, I already mentioned the assistance they provided that led to a criminal prosecution for bid rigging at a Nebraska cattle auction, and in the Cargill/Continental merger investigation. In other examples, we received useful market information from GIPSA during our investigations into the lamb industry a few years ago, as well as during our investigation into other recent mergers. We have consulted with GIPSA in connection with its investigation of federal cattle procurement practices, and helped advise GIPSA in shaping and overseeing recent economic studies of agricultural market concentration issues. Last summer, together with the Federal Trade Commission, the Antitrust Division and USDA signed a Memorandum of Understanding Relative to Cooperation With Respect to Monitoring Competitive Conditions in the Agricultural Marketplace that ensures that they will share information as appropriate and "confer regularly . . . consistent with applicable confidentiality restrictions, to discuss law enforcement and regulatory matters related to competitive conditions in the agricultural marketplace."[4]

Conclusion

When someone from the Antitrust Division speaks about our work, we try to make clear to everybody that if they have any information that they think is relevant to our enforcement activities,

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[3] We also required Cargill to enter into what is called a "throughput agreement" to make one-third of the loading capacity at its Havana, Illinois, river elevator available for leasing to an independent grain company, and are imposing restrictions on Cargill in the event it seeks to enter into a throughput agreement with the operator of the Seattle facility.

[4] The Antitrust Division shares antitrust enforcement responsibility with the Federal Trade Commission, with a few exceptions (e.g., criminal enforcement under the Sherman Act is exclusively in the Antitrust Division; and by tradition the FTC handles enforcement of the Robinson-Patman Antidiscrimination Act).

we want to hear about it. As a law enforcement agency, we treat conversations with us in confidence. If the information leads us to conclude that the antitrust laws have been violated, we will take appropriate enforcement action. In the meantime, we will continue monitoring this industry closely.

The Antitrust Division takes seriously its responsibility to protect the marketplace – including the agricultural marketplace – against anticompetitive conduct and mergers that substantially lessen competition. As I hope I have made clear, the Division has a record of acting in this important sector when the antitrust laws are violated.

THE CASE AGAINST AN "AGRARIAN ANTITRUST POLICY"

F. R. Warren-Boulton
Principal,
MiCRA: Microeconomic Consulting and Research Associates, Washington, D. C.

Those who argue in favor of a new and more expansive "Agrarian Antitrust" policy (e.g., Professors Christenson, Lauck[1], and Harl[2]) express three concerns that they believe could and should be addressed by more active antitrust enforcement in the agricultural sector. The first is the failure of current antitrust policies to adequately take into account monopsony power directed against farmers, and to block mergers that increase such monopsony power -- a failure rooted in a value judgement that antitrust should be concerned only with the welfare of consumers and should ignore the welfare of suppliers. The second is the absence of non-economic considerations such as the preservation of the family farm and less concentrated market structures at other levels, and the third is the spread of contract agriculture.

I MONOPOLY AND MONOPSONY AS A CONCERN FOR MERGER AND ANTITRUST POLICY

Several writers calling for an "Agrarian Antitrust" policy seem to believe that farmers have been short-changed or even abandoned by current antitrust policy.

They note that the major concern for farmers is, and has always been, <u>monopsony</u> power, i.e., when many suppliers face one buyer (monopsony) or only a small number of buyers (oligopsony), resulting in lower prices to farmers.

The argument seems to be that the agencies are concerned only with <u>monopoly</u> power – one or a few sellers – which results in higher prices to consumers. Somehow, the interest of suppliers has been forgotten – only consumers count.

I have three points..

First, as an economist, I agree that monopsony and monopoly are twin evils:

> Both monopoly and monopsony transfer wealth (usually from lower to higher-income individuals)

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[1] See, e.g., Lauck, Jon, "Toward an Agrarian Antitrust: A New Direction for Antitrust Law" *North Dakota Law Review* 75:449, 1999.

[2] See papers listed at http://www.econ.iastate.edu/faculty/harl

and,

> Both monopoly and monopsony result in lower output/production, less inputs purchased, higher prices to consumers, and lower prices to suppliers.

Incidentally, most normal people (i.e., non-economists) believe that since monopsony results in lower prices for inputs, it must also result in lower prices to consumers. But in fact, the reverse is true. When firms with monopsony power drive down supplier prices, they do so by restricting their purchases of those inputs. Less inputs means less output. Less output means higher prices to consumers. The gross margin of the monopsonist increases both because the price he charges for his output goes up and the prices he pays for his inputs go down.

Probably the best known current example of monopsony is in sports: the reserve clause, which prevents teams from bidding up the salaries of players. (Earlier version was known as slavery). Many fans support this, believing, erroneously, that this somehow results in lower ticket prices. Unfortunately, it only benefits the team owners.

But, second, both are opposed equally under current Agency antitrust merger policy. The Merger Guidelines, the "Bible" of antitrust policy, says:

> Market power also encompasses the ability of a single buyer (a "monopsonist"), a coordinating group of buyers, or a single buyer, not a monopolist, to depress the price paid for a product to the level that is below the competitive price and thereby depress output. The exercise of market power by buyers ("Monopsony power") has adverse effects comparable to those associated with the exercise of market power by sellers. In order to assess potential monopsony concerns, the Agency will apply an analytical framework analogous to the framework of these Guidelines. (*Merger Guidelines*, SS 0.1).

And the Federal and State antitrust Agencies follow up on this by actively enforcing anti-monopsony policies:

As an example, BP and ARCO are by far the two largest bidders on state oil lands in Alaska – Alaska is, in effect, a two-company state. The State of Alaska was about to move to block the BP-ARCO merger on the grounds that it would create monopsony power in the market for oil leases in Alaska, resulting in lower bid prices and less state revenue from leasing. The State of Alaska -- the primary "victim" of such monopsony power – reached an agreement with BP-ARCO on terms that it believes were highly advantageous to the State.

Now the FTC has decided to challenge the merger anyway, apparently at least partly in the belief that the State has not gone far enough in protecting its own self interest. So it's hard to argue that the Federal Agencies aren't going far enough to prevent monopsony power when they seem to be going further than even the potential victims want them to go.

Similarly, the DOJ imposed a number of conditions on the Continental Cargill merger that seem to go beyond what would have been indicated by the *Guidelines* or what most observers would have expected.

Third, many cases that look like monopoly cases, and are characterized that way, are actually monopsony cases. Take the example of two competing railroads that connect a group of farms producing a given crop with a destination where that crop is processed or consumed.

Railroad A ------------------------------Railroad A

FARMS (SUPPLIERS)

CUSTOMERS (PROCESSORS OR CONSUMERS)

Railroad B------------------------------Railroad B

Suppose we examine a merger of these two railroads. Most economists – and even non-economists – would analyze this merger in terms of a "Demand for transportation". The demand curve for transportation of this commodity (say, wheat) from farmers to customers/consumers would look like Fig 1. It is downward sloping because an increase in the price of transportation (the railroad tariff) will result in a reduction in quantity -- the amount shipped.

Suppose that this merger would result in higher RR tariffs (from t_0 to t_1) and reduced shipments (from Q_0 to Q_1). Where does that higher tariff come from? The tariff is just equal to the difference between the price of the commodity at the origin and the price of the commodity at the destination. So if the tariff goes up, either the destination price goes up (higher prices to consumers) or the origin price goes down (lower prices to suppliers) or both. (See Fig 2)

Who bears the cost of the tariff increase? That depends on which end -- suppliers or consumers -- had the most alternatives. The tariff increase could be born entirely by farmers (as in Fig 3) if consumer demand is highly elastic (because consumers have many other sources for the commodity) while supply elasticity is low (because farmers have no other outlet for their crop). Or it could be born entirely by consumers (as in Fig 4) if consumer demand is inelastic (because they have no other source of supply for the commodity) while supply elasticity is high (because farmers have many other outlets for their crop). Or the burden of the higher tariff could be shared between suppliers and consumers.(Fig 5).

The antitrust laws and current antitrust policy do not differentiate or discriminate. If the merger of two railroads would result in a higher rail tariff, antitrust enforcers do no ask how the cost would be shared between suppliers and consumers. The merger would not be approved either if all the costs were born by suppliers, or if all the costs would be born by consumers

Most of us, I believe, would oppose such discrimination on principle. It is difficult to see how such a policy could be "just" in a Rawlsian sense, i.e., to rationally support a policy that concerned itself with only the welfare of consumers or only the welfare of suppliers would require that one knew whether one was a supplier or a consumer. So the position becomes the old "where I stand depends on where I sit". Quite understandable, but not a very ethical position..

Most economists would also oppose this kind of discrimination, not because they oppose income redistribution *per se*, but because experience has shown that antitrust is a grossly inefficient and ineffective way to redistribute income. We would argue that the best approach is to use antitrust (and regulation where antitrust alone cannot create a competitive structure, i.e., where economies

of scale are so large as to create a "natural monopoly") to create something as close as possible to a competitive equilibrium - to mimic what would happen under perfect competition – since that maximizes the size of the pie. We (society) can then look at the resulting income distribution, and if it is unjust, redistribute income on an individual basis in the most efficient way possible. Redistribution by occupational class is inherently unjust (why should a small business owner -- say, a dry cleaner operator Washington – be treated differently than a farmer in Iowa with the same income?). And antitrust is a grossly inefficient way to redistribute income. It is also ineffective: anyone who thinks that government actions that depart from transparency and a rule of law will favor the poor and the weak, much less the small family farm, probably hasn't spent much time in DC.

II. CONSUMER WELFARE OR TOTAL WELFARE?

The real threat to full consideration of the interests of suppliers (such as farmers) comes from those who argue for a strict "consumer surplus only" standard, as opposed to the "total welfare" standard assumed above. Under a consumer surplus standard, only the welfare of consumers *as consumers* is valued. Thus, in mergers, efficiencies are not recognized/counted/cognizable unless and to the extent that they are "passed through" to consumers in the form of lower prices. This was not the policy position in the Reagan administration, but has been the Agencies' official position recently in court (e.g., in *FTC v. Staples and Office Depot.*), and is the hallmark of the "consumer surplus" approach to merger enforcement (e.g., see Lande[3])

Those, such as Lauck, who argue for an Agrarian Antitrust, also argue for a merger standard under which efficiencies from a merger are discounted or not even counted unless they are "passed on" to consumers. Such a "only consumer surplus counts" standard may seem appealing because ignoring efficiencies from mergers would be against the interest of "agribusinesses" such as Cargill or DuPont. But to the extent that they are successful (as they have increasingly been among lawyers -- as opposed to economists -- in the recent administration) in persuading attorney policymakers at the Agencies that the interest of one set of suppliers (i.e., the interest and welfare of shareholders in merging firms) should not be taken into account, they inevitably force the policymaker into also excluding the interest of other suppliers (e.g., farmers). Neither shareholders in Continental nor farmers are consumers *qua consumers*. Ultimately, if we continue down this road, neither farmers nor shareholders will count except as diners.

III FARMERS AS SERFS AND THE "ALIENATION OF THE AGRICULTURAL PROLETARIAT"

Finally we come to higher values: the agrarian ideal of the family farm. In antitrust, these kind of sentiments have bee most famously reflected in Judge Hand's oft-cited dicta:

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[3] Alan A. Fisher and Robert H. Lande, Efficiency Considerations in Merger Enforcement, 71 Cal. L. Rev. (1983) and other papers cited in Lauck, op. cit..

> It is possible, because of its indirect social or moral effect, to prefer a system of small producers, each dependent for his success upon his own skill and character, to one in which the great mass of those engaged must accept the direction of the few:" (Learned Hand, 1945).

I do not doubt that many individuals value independence and self-direction. Many people work for themselves, or in small business, or on family farms, for far less than they could earn by working on salary for a large corporation. When I and a few friends started a small consulting firm a few years ago, everyone told us that we could earn far more by joining one of the large consulting companies. They were right, and we knew it.

I greatly valued the right to make that choice for myself, but I assume that I would bear the costs. Why should anyone else pay them? To paraphrase Judge Hand, why would anyone,

> "because of its indirect social or moral effect,... prefer a system of small consulting firms..., to one in which the great mass of economists must accept the direction of the few"?

And do farmers really want their representatives to block mergers among agricultural firms if that meant lower income to farmers, just to live in a less concentrated market? Consider *Cargill v. Montfort*. There, the merger of Cargill and Spencer was challenged by a competitor, Montfort, who claimed that the efficiencies from the transaction would result in increased output by the new, more efficient firm. Cargill-Spencer would sell more beef and buy more cattle. This would result in lower beef prices to consumers, and higher cattle prices to ranchers. But higher prices for cattle would harm Montfort. The plaintiff's position was that a merger among two of his competitors should be blocked <u>because</u> it would result the plaintiff's having to pay higher prices to cattle ranchers.

Banning this merger on the principle that higher concentration in agribusiness is "bad", regardless of its economic effect, would clearly have harmed farmers. Do farmers really want an antitrust policy whose goal is to help competitors, rather than competition, consumers and suppliers? Once you invite that bear into your house, it is more likely to eat the farmers than feed them.

One noted academic advocate of an Agrarian Antitrust -- Jon Lauck - commented that

> The remarkable aspect of the case is that suppliers of cattle to the newly-merged firm did not protest the merger. (Lauck, p.504)

Such a failure to protest higher incomes would not come as a surprise to any economist, but then perhaps we lack an appreciation for the higher things in life. And then, perhaps real farmers share our values more than those who purport to represent them.

IV CONTRACTS, ANTITRUST, FREEDOM, AND THE TYRANNY OF THE COMPETITIVE MARKET

Agrarian Antitrust proponents also express concerns as to new contractual relationships between farmers and business, especially hi-tech businesses such as Monsanto and DuPont, referring to "vertical contracts" that create barriers to entry and "intellectual property abuse."

To the extent that such arrangements are in fact anticompetitive, they would violate the antitrust laws and could be expected to be treated as severely as in any other sector of the economy.

One potential source for such concerns, however, would not be covered by antitrust. Many family farms that recently entered into contracts for products such as hogs and chickens and incurred substantial sunk costs suffered from "opportunistic behavior" by the firms with whom they had contracted. They presumably still have recourse in the law, but as a contract violation. No Agrarian Antitrust, however active, wold be relevant to these cases.

But the proponents of an Agrarian Antitrust go beyond such "economic" arguments to argue, again, that such arrangements transform the farmer or rancher "into a mere servant or agent of a corporation" (Carstensen, citing Peckham).

Almost by definition, contractual relationships involve less fiat than vertical integration -- farmers facing markets have more discretion than facing a human boss. But a competitive market can be even a tougher boss than a human one, especially when the product is a "commodity," so that one farmer's product is just like any other, every farmer is in competition with every other farmer, and only the lowest cost, lowest price producer survives.

One potential escape from such bondage for commodity grain producers might be offered by specialty grains. Unlike hogs and chickens, which require substantial sunk costs which expose the farmer to opportunistic behavior by downstream firms, specialty grains require no additional investment for the farmer other than an additional bin to hold grain. Product prices for specialty grains would be higher than for commodity grains, and the product is differentiated, and the number of suppliers of each specialty far fewer than for commodity grains.

Perhaps again, what seems to the observer as servitude may in fact be freedom to the farmer.

Fig. 1

Demand for Transport

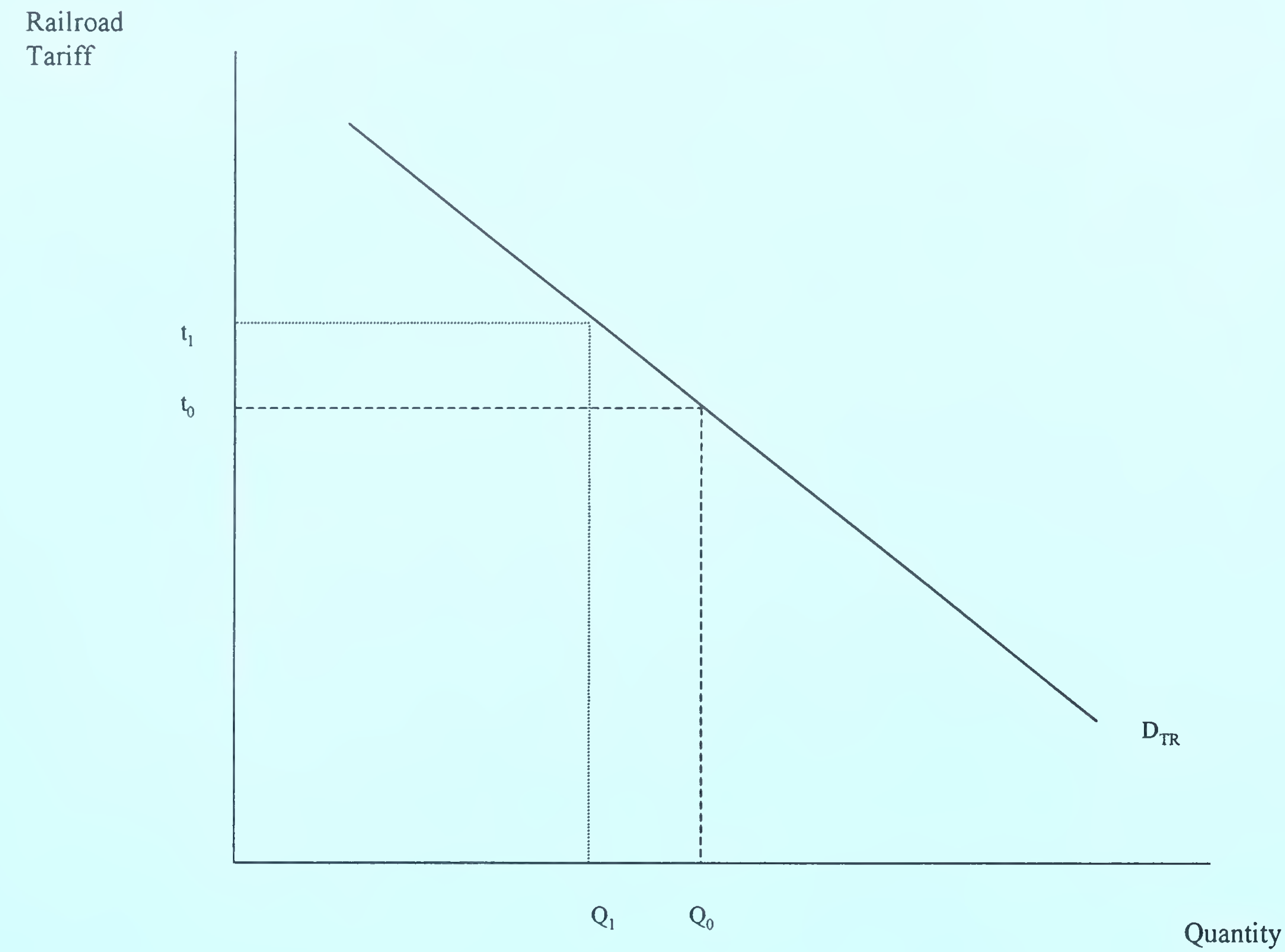

Fig. 2

Supply (at farm) and Demand (at city) with Railroad tariff as "wedge"

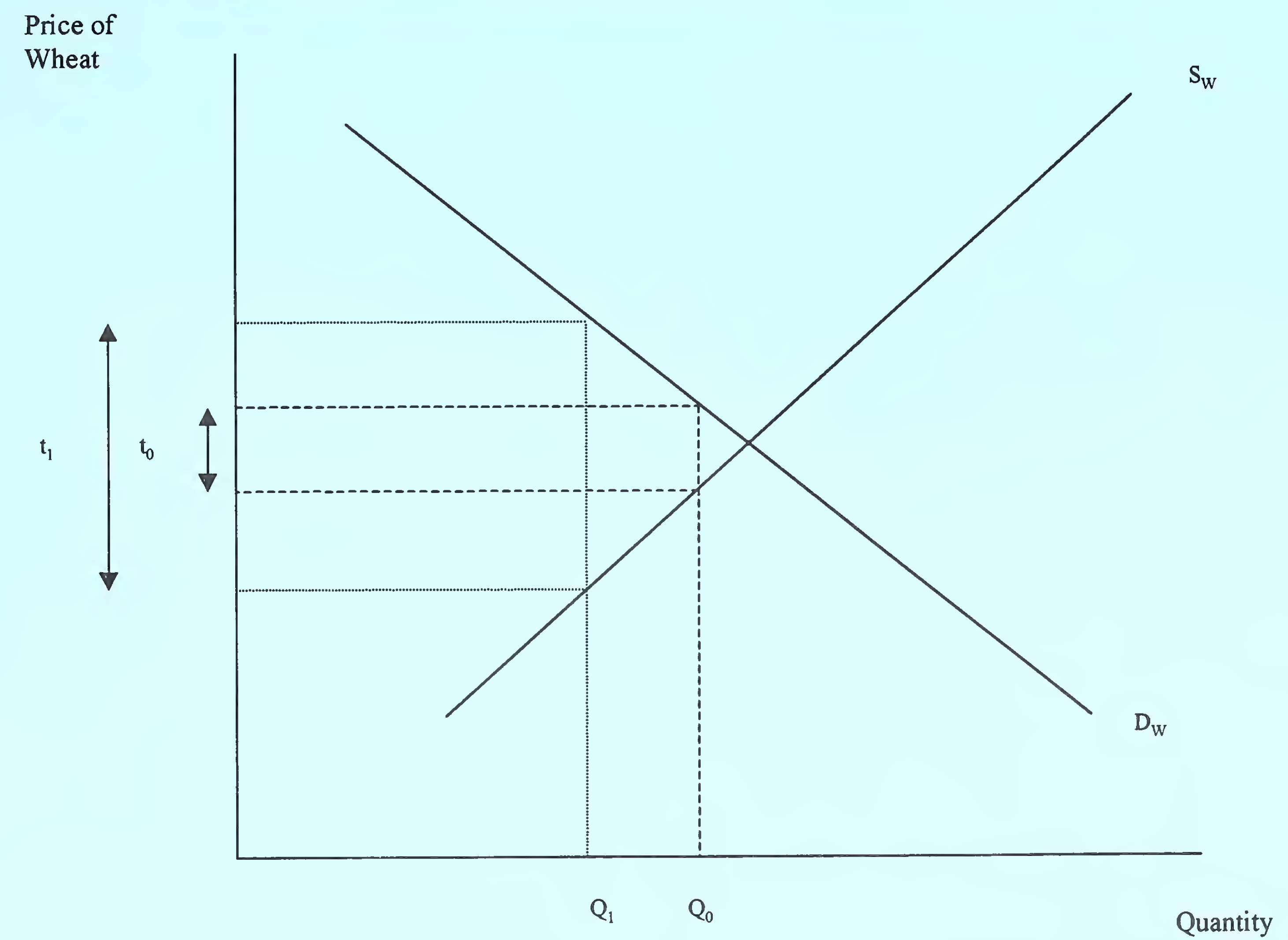

Fig. 3

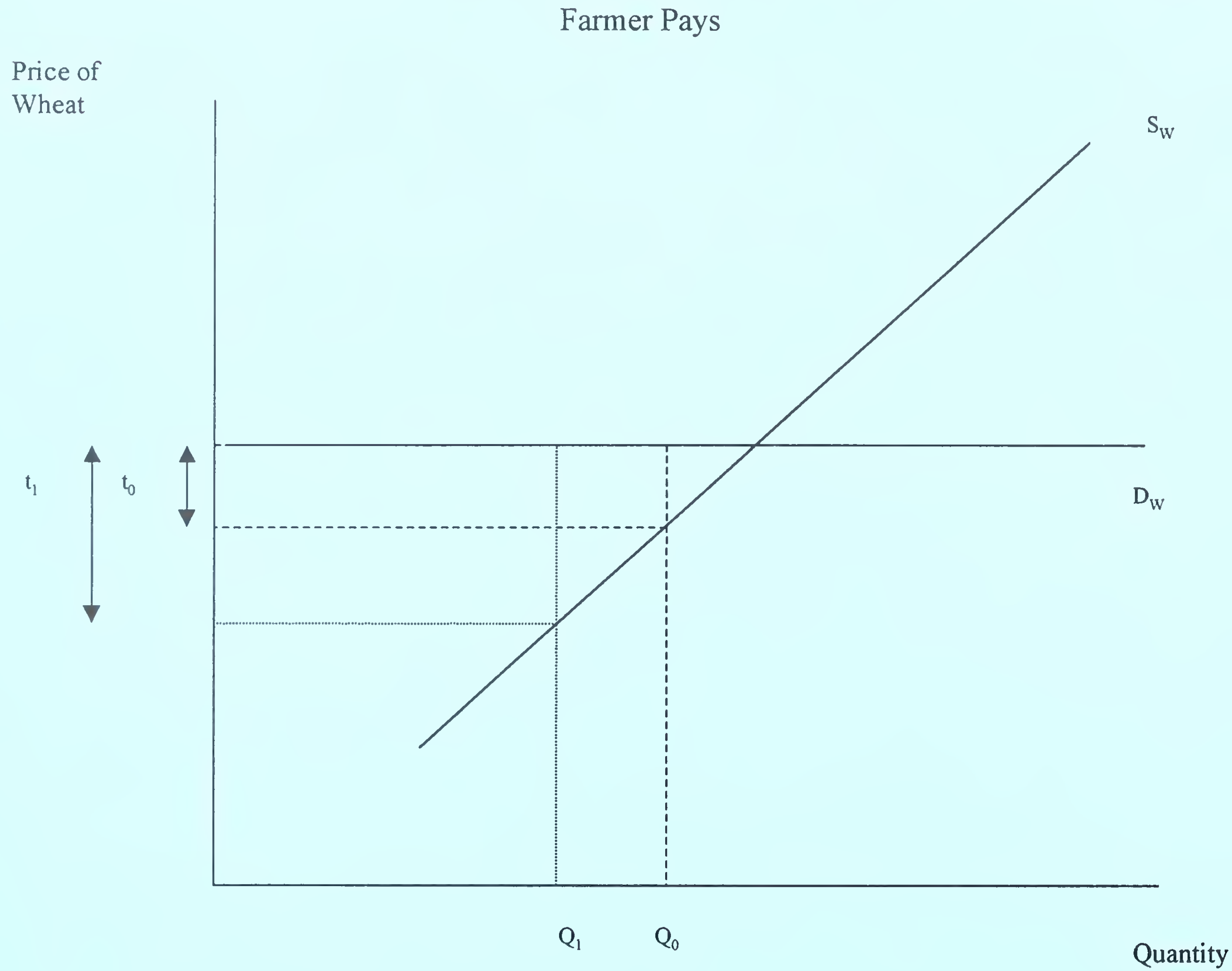

Fig. 4

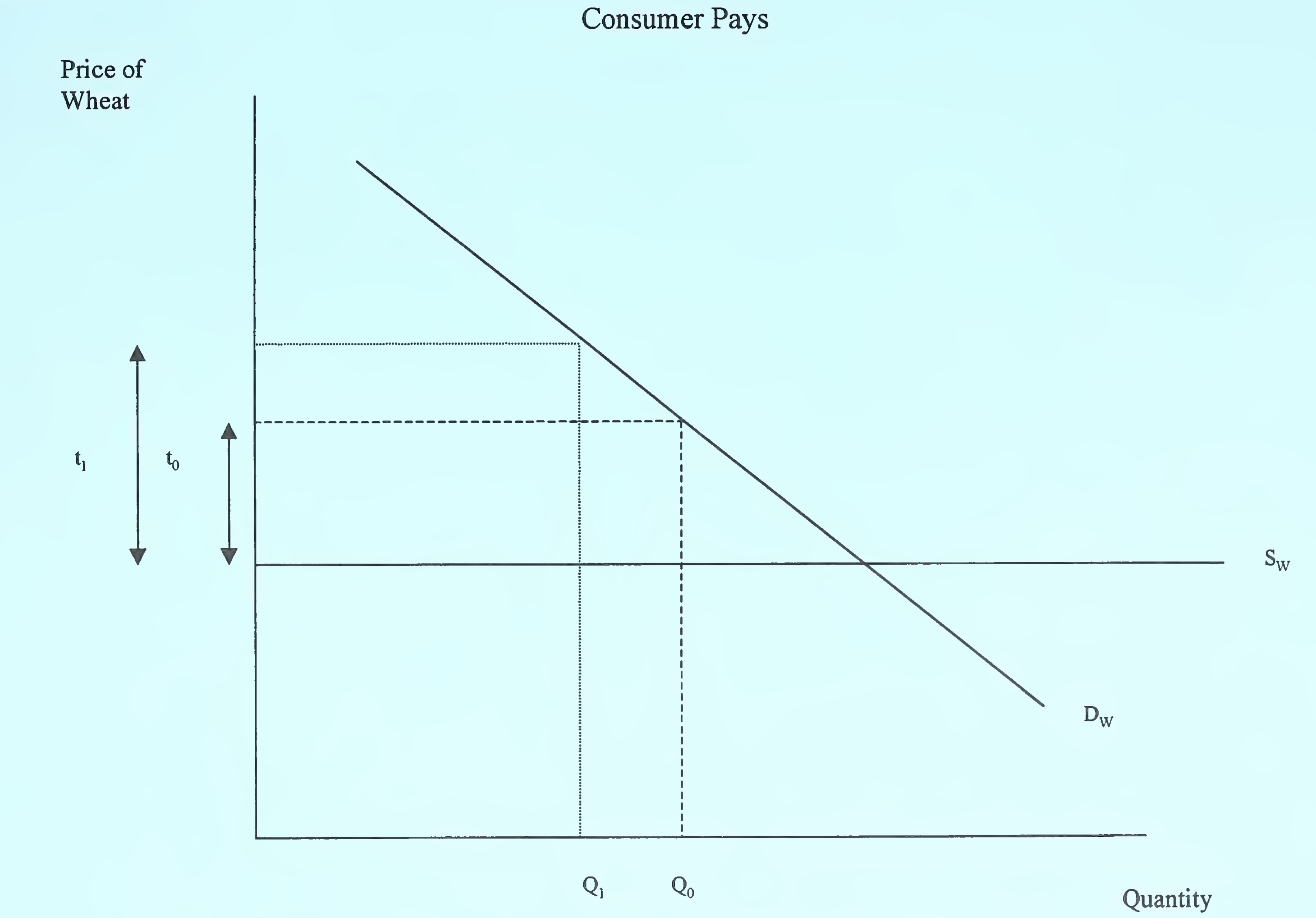

Fig. 5

Both Pay